Excerpt: Taxes and Economic Growth page 16

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PBot inside

Intellectual Ammunition

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Potshots

When the press tells us what issues obsess the American people, they're really talking about the issues that interest the journalists, pundits, and politicians.

HARRY BROWNE

Even if you're on the right track, you'll get run over if you just sit there.

WILL ROGERS

Bipartisan consensus is like when my doctor and my lawyer agree with my wife that I need help.

MATT BEAUCHAMP

Political people are adroit at arguing that anything and everything that happens, or does not happen, demonstrates the wisdom of whatever they want.

GEORGE F. WILL

The grand essentials of happiness are: something to do, something to love, and something to hope for.

ALLAN K. CHALMERS

There is no luck except where there is discipline.

IRISH PROVERB

Bumper Snicker: Taxation WITH representation isn't so hot, either!

Give the States Back Their Money

by William B. Conerly, Ph.D.

With employment declining in most states, it's time for the federal government to quit taxing employment just to limit the federal deficit.

Employers in the 50 states send $6.8 billion to Washington, DC in federal unemployment insurance taxes every year. The money is supposed to go back to the states for administration of the unemployment insurance system and for other related programs ... but less than half of the funds ever get out of the Beltway. Congress has been keeping the money piling up in trust funds to show a smaller overall budget deficit.

Fortunately, the Bush administration has shown some common sense with proposals to free up the employment tax revenue.

WHAT IS FUTA?

The federal unemployment insurance tax (called FUTA, after the Federal Unemployment Tax Act) is collected from employers in every state. Funds are sent by employers to Washington, then returned to the states for administrative expenses. The money also provides trust funds for loans to states and for the "federal share" of extended benefits, a program that kicks in when unemployment is unusually high.

Only 47 percent of the money collected from employers was expended in 1999, the most recent year for which data are available. The rest of the money stays in federal trust funds to limit the budget deficit (or formerly, to build up the surplus).

All of this is separate from the state unemployment insurance tax, which goes into state unemployment insurance trust funds, which provide the actual benefit payments to unemployed workers.

Even though the FUTA taxes are earmarked for a specific purpose, the federal government calculates the revenue as part of its total income. Appropriations from the trust fund are counted as expenditures. In other words, returning these funds to the states increases the budget deficit. Congress thus taxes employment for a specific program, but spends little of the revenue on any program at all.

The FUTA tax is 0.6 percent of each employee's wages (up to $7,000 of wages a year). Congress added a 0.2 percent surtax to replenish the trust fund after the recession of 1973-75. The replenishment has been accomplished, and then some ... but Congress maintains the surtax, for a total tax rate of 0.8 percent. Why? To keep that federal deficit from growing too large.

WHAT'S WRONG WITH THIS PICTURE?

The federal trust fund is created by a tax on jobs. The strategy we have used to reduce cigarette

continued on page 3

CONTENTS

Education	5	Regulation	11
Environment	6	Taxes	12
Health Care	7	Technology	13
Law	8	Welfare	14
Privatization	10	Excerpt	16

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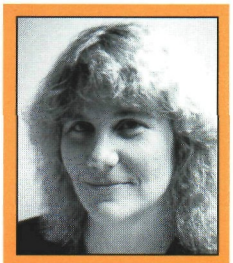

News from the Heartland

by Diane Carol Bast
Editor

As the 2002 campaign season ramps up, this issue of *Intellectual Ammunition* offers a wide range of "tools for political survival"—resources candidates and grassroots activists can use to build public support for their positions and principles.

SPEECHES, NEWSLETTERS

I recently heard a speaker open up with, "I understand I'm supposed to start my speech by getting everybody to laugh. But I'm not a funny guy. So will you please all laugh right now so we can get on with it?"

The ploy worked, but he should have had this issue's Potshots. They're perfect openers for a campaign stump speech; great "filler" for a newsletter; and handy for "quotes of the day" on your Web site or in your emails. Hundreds of other jokes and quotes can be found on Heartland's Web site. Click on *PolicyBot* and search the "Humor" Topic.

For more "meaty" stuff, any one of this issue's columns would make a great article for a newsletter or to send along with a letter or position statement. Nurse Twila Brase's Health Care column, ten tips for better understanding health insurance coverage, especially fills the bill.

You have blanket permission to reprint Twila's column and every other column in this issue. Please include a statement along these lines: *Reprinted from the May/June 2002 issue of Intellectual Ammunition, published by The Heartland Institute.*

POLICY PROPOSALS YOU CAN SUPPORT

In this issue's cover article, William Conerly says it's high time the federal government quit taxing jobs in your state, just to cover up its own deficit spending. The Bush administration has expressed its openness to reforming the federal unemployment insurance (FUTA) tax scheme. States should adopt resolutions expressing their support for FUTA reform as a way to stimulate their state economies.

Teresa Bauman's excerpt of a report by economist Richard Vedder, published by the Cedarburg, Wisconsin-based Taxpayers Network Inc., also focuses on economic growth. Vedder evaluates each state's tax policies to determine whether they promote economic prosperity for their citizens. How does your state rank? What can you do to improve your position?

THINK TANKS YOU CAN RELY ON

All of *Intellectual Ammunition*'s regular columnists work for organizations whose mission is to help you make better-informed public policy decisions. We also offer in this issue a directory of more than 150 think tanks, legal foundations, and advocacy groups The Heartland Institute regularly works with.

COOL OFF WITH US

There are ads in this issue for ice cream socials Heartland will be sponsoring at the mid-summer annual meetings of the American Legislative Exchange Council and National Conference of State Legislatures. Heartland Publisher Nikki Saret and Public Affairs Director Greg Lackner will be on hand to answer any questions you might have about Heartland's work. And these are family affairs ... so please bring children and spouses! We promise a good time will be had by all.

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continued from page 1

and alcohol consumption—taxing them heavily—is also being used to limit employment. The only problem is that in a recession, we want *more* jobs, not fewer.

There is some logic in taxing employment to administer the unemployment insurance system. But where is the logic in collecting the taxes but not spending the money?

State efforts to help the unemployed are stifled by the FUTA system. The formula for distributing administrative monies from the federal trust fund to the states is based on workloads, such as processing claims, hearing appeals, and distributing checks. States that do a good job getting people back to work lose funding.

HOW TO RETURN THE MONEY

The first step in returning the money to the states is for the federal government to stop collecting it.

After the 0.8 percent federal tax is eliminated, states could levy a tax averaging only 0.4 percent of wages and cover their own administrative expenses. The exact amount would vary from state to state.

Every state already collects unemployment insurance taxes from employers. It would be a simple matter to add on the state administrative tax. No extra forms or paperwork would be required of employers. The only change—a change for the better—is that they would no longer have to file federal forms in addition to their state forms.

Returning the existing trust funds to the states is the second step. The total amount in the federal trust funds is now about $23 billion: seven times the annual administrative expenses paid by the federal government. The states could use their distribution to bolster their state unemployment trust funds, which pay the actual benefits to the unemployed. With that addition to their own trust funds, states could afford to delay implementation of the new administrative tax until recovery from the recession is complete.

In addition to paying for administrative expenses, some of the FUTA tax goes into a trust fund that provides loans to states that run out of money in their state unemployment insurance fund. The last such loans were made in 1993.

As a source of loan funds to the states, the federal trust fund is expensive. Interest is charged at a rate equal to federal borrowing costs. States, however, can borrow at lower rates, because of the tax-exempt status of state debt. For example, on March 4, 2002, states were paying, on average, 2.18 percent on bonds of two-year maturity, while the federal government was paying 3.24 percent. It's no bargain for the states to be able to borrow from the federal government at federal cost.

If a safety net is needed, states can agree to borrow and lend among themselves. Even during the worst recessions, the positive trust fund balances of healthier states have exceeded the deficits of weaker states. Further, the federal government could just lend from the U.S. general fund to the states as an ultimate safety net.

The final function of FUTA is to provide the "federal share" of extended benefits. The extended benefits program increases the maximum duration of benefits, from the normal 26 weeks to 39 weeks. It goes into effect when a state's unemployment rate increases to an abnormally high level.

Officially, half the benefits come from the state, and half from the federal government. But the federal half comes from money collected from the tax on jobs in every state. There is no separate honey pot of funds for the federal expenditures: The money really comes from the states.

The strategy we have used to reduce cigarette and alcohol consumption—taxing them heavily—is also being used to limit employment.

Most states got through the severe recession of the early 1980s with enough in their state reserves to cover their own share of extended benefits as well as the federal share. Had the state trust funds been bolstered by money that actually went to FUTA, even more states would have avoided the need to borrow from the federal government.

But what of those states that did need additional funds to get through the recession? Extended benefits could be protected in three different ways: 1) interstate loan agreements; 2) general borrowing, to be repaid by the state unemployment insurance trust fund when employment rebounds; or 3) loans directly from the federal government. It is not necessary for the federal government to sit on money to protect the states' ability to pay benefits.

BENEFITS OF RETURNING TRUST FUNDS

Every state is likely to enjoy greater employment, at least to a small extent, from elimination of FUTA. In addition, some states are likely to experiment with better ways to serve the unemployed, since doing so would not result in reduced administrative funding. Some of those experiments will certainly work, and then be copied by other states.

It's also possible that by spending more on helping the unemployed find jobs faster, we can save an even greater amount in benefits. For instance, job search seminars have, in some cases, proved cost-effective: The expense of the seminar was outweighed by the payments saved because of more rapid re-employment. Today, states cannot make tradeoffs between administration and benefits funds. If FUTA were eliminated, states would likely save money by providing better services to the unemployed.

Finally, eliminating FUTA will substantially reduce the administrative burden on business, which hits small business especially hard. Employers today have to file two tax returns, one to the federal government and one to the states. The forms are different, and the filing deadlines may be different. The administrative burden is one factor making small businesses hesitant to hire staff. Total employment is quite likely to improve with this burden removed.

TIME TO CHANGE

The federal unemployment insurance tax has been a bad idea for years, but it was a bad idea we could afford. Now, in recessionary times, we cannot afford to tax jobs just to maintain the federal surplus.

The Bush administration's budget proposal calls for reform, though not quite as thorough-going as this article suggests.

Under the Bush plan, the FUTA tax would be gradually cut from 0.8 percent of wages to 0.2 percent. States would finance their own administrative services, presumably raising their own state taxes enough to compensate for the lack of federal administrative money. Some of the accumulated trust funds would be returned to the states for transition costs to the new system. The federal government would continue to make loans to states that run short of funds to pay benefits.

Although not perfect, the Bush proposal is a major step forward for the unemployed, returning most of the FUTA money to the states and stimulating better ways to help the unemployed.

William Conerly is an economic consultant in Portland, Oregon. He can be reached at Bill@ConerlyConsulting.com. *This research was supported by the American Institute for Full Employment.*

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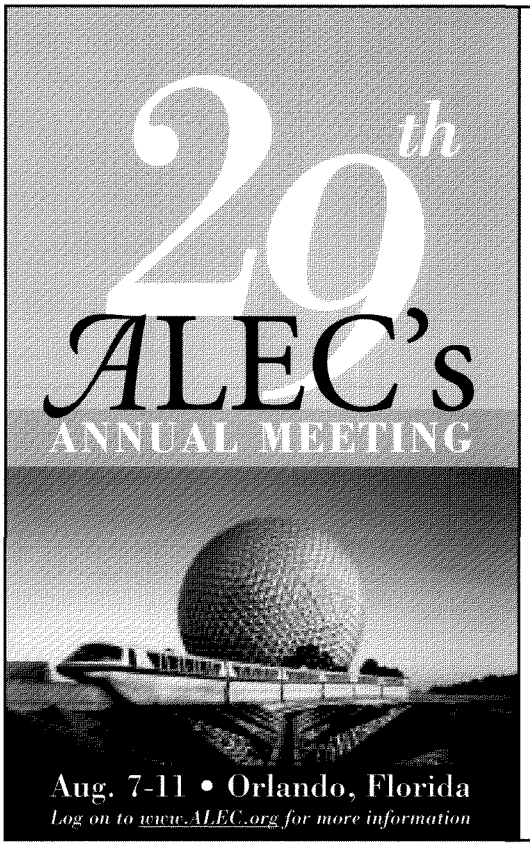

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Education

What Should We Expect from Smaller Classes?

George A. Clowes

George A Clowes is managing editor of *School Reform News*, a publication of The Heartland Institute.

While recognizing that "class-size reduction has lately gone from being a subject of primary academic interest to a policy juggernaut," a group of international researchers last November recommended legislators consider lower-cost alternatives—such as attracting better teachers—"before they commit billions more on reducing classes across the board."

In a thoughtful review of studies of class size and academic performance in last November's *Scientific American*, Ronald G. Ehrenberg and colleagues point out class-size reduction has one obvious drawback: "It costs plenty." They note the state of California alone has spent more than $1.5 billion annually over the past several years to reduce class sizes to 20 or fewer in kindergarten through third grade ... with only a "tiny effect."

The impact achieved by another class-size reduction experiment—Wisconsin's SAGE (Student Achievement Guarantee in Education) program—is much greater than that seen in California, but SAGE is not just about reduced class sizes. SAGE is a targeted intervention program aimed at raising the academic achievement of disadvantaged children not only by reducing class sizes to 15 in kindergarten through third grade, but at the same time implementing a rigorous academic curriculum, providing before- and after-school activities, and implementing professional development plans.

> *"California alone has spent more than $1.5 billion annually over the past several years to reduce class sizes to 20 or fewer in kindergarten through third grade ... with only a 'tiny effect.'"*

Students in classrooms adopting this four-part intervention package show a significant performance advantage over students in non-SAGE classrooms in all grades, although the gains do not widen over time. However, the most significant finding emerging from the SAGE experiment is the overriding importance of good teachers and good teaching techniques.

MINIMIZING DISRUPTIONS

How do small classes actually work to produce improved student performance? The conventional wisdom is that small classes "minimize disruptions."

The effect of reducing disruptions in a classroom has been analyzed by Edward Lazear, an economist at the Hoover Institution and Stanford Graduate School of Business. Lazear was interested in how disruptions by individual students affect the time available for learning for the class as a whole. His basic model calculates the available learning time as the time remaining after disruptions.

For example, Lazear's model shows that if each student in a class of 30 disrupts the class 1 percent of the time, only 74 percent of class time is available for learning. That's because each student's disruptions reduce the available learning time for all other students.

Lazear's model permits an estimation of the gain in learning time from reducing class size for different levels of student disruption. For example, in classes where each student is disruptive 2 percent of the time, the available learning time for a class of 25 is 60 percent of total class time. Reducing the class size to 15 increases the amount of learning time to 74 percent, a gain of 23 percent in learning time. Although each student is just as disruptive as before, the disruptions affect fewer students and there are fewer students to be disruptive.

The more disruptive the class, the greater the gain in learning time when class size is reduced. At a 5 percent level of disruption, the gain in learning time from reducing class size from 25 to 15 is a spectacular 64 percent, from 28 percent to 46 percent. Conversely, the less disruptive the class, the smaller the gain in learning time when class size is reduced. At a 1 percent level of disruption, the gain in learning time from reducing class size from 25 to 15 is 10 percent, from 78 percent to 86 percent.

POLICY IMPLICATIONS

If the aim is to increase the amount of time available for learning, this may be achieved in two ways: either by reducing class size, or by enforcing greater discipline in the classroom.

In a class of 25 students, reducing the level of student disruption from 5 percent to 3 percent increases the amount of available learning time by 68 percent, the same gain that would be achieved by keeping the disruption level constant and reducing class size to 15.

Discipline is a substitute for class size. This has significant policy implications, since the cost of reducing class size is very much greater than the cost of teaching an educator improved classroom management techniques. As the last two years' reports from the SAGE experiment have shown, the impact of different teaching styles on student achievement is substantial, independent of class size changes.

FOR MORE INFORMATION...

Should Classes Be Smaller ... Or Simply More Orderly? Economist Edward Lazear's work on the value of minimizing classroom disruptions is explored in further detail. (*School Reform News*, September 2001, 3pp.)

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Environment

Dr. Jay Lehr

Guest columnist Jay Lehr Ph.D. is science director for The Heartland Institute and president of Environmental Education Enterprises.

GM Corn Protest Based on Bio-Fraud

Environmental and consumer groups staged protests and held news conferences across the country in April to call attention to their claim, as one news release put it, that "the genetic contamination of Mexican native corn varieties threatens not only the genetic integrity of corn, one of the world's most important basic crops, but the food security for millions in the Americas."

The statement is false ... and even its author knew it was false at the time it was written. The protest was based on claims that have been debunked by the scientific community. It aimed at exploiting the ignorance of citizens and policymakers. It is an example of bio-fraud, an all-too-common tactic of radical environmental groups.

JUNK SCIENCE

In a letter to the editors of *Nature* published last November, a scientist with a history of anti-technology advocacy and his assistant claimed to have tested samples of corn grown on farms in Southern Mexico. They reported that by using genetic tests, they had found the local corn was "contaminated" by genetically modified corn.

> *Environmental advocacy groups cannot be trusted to tell the truth. Their alarmist rhetoric damages the scientific process and costs badly needed jobs and export income.*

Three groups of university-based scientists, working independently, examined the research data and found it to be erroneous. Each group submitted formal letters to *Nature* challenging the letter's validity. In addition, the editors of the *Transgenic Research Journal* examined the data and determined it to be "fundamentally flawed." On March 1, a petition signed by nearly one hundred prominent scientists was released, calling for greater scrutiny of the report.

In a comprehensive review of the controversy published in the February issue of the *Transgenic Research Journal*, the Center for the Improvement of Maize and Wheat in Mexico stated, "no credible scientific evidence is presented in the paper to support claims made by the authors that gene flow between transgenic maize and traditional maize landraces [strains] has taken place." The reviewers found it "most frustrating" that the authors failed to use more reliable techniques to determine the presence of the transgenes.

An editorial note in the late March edition of *Nature* officially ended the scam: "*Nature* has concluded that the evidence available is not sufficient to justify the publication of the original paper."

SPREADING THE LIE

Even as the claim at the base of the controversy was being debunked, environmental groups were spreading the lie to media outlets around the world. Hundreds of newspapers carried the false report. Few are ever likely to print retractions.

Using the false data, Greenpeace and other activist groups persuaded the Mexican Interior Ministry in February to consider modifying the existing Federal Penal Code to severely penalize anyone engaged in the introduction, commercialization, transportation, storage, or release into the environment of any genetically modified organism. Punishment would include imprisonment for one to nine years and a fine from 300 to 3,000 times the minimum daily wage of those convicted of such an offense.

The economic implications for America's farmers and agribusinesses are considerable. The U.S. exports to Mexico over $600 million worth of corn and about $100 million worth of processed corn products, such as high fructose corn syrup, annually. Markets in other countries where biotech is an issue are also being affected.

In addition, environmental groups used the faked study to kick off April's "Continental Campaign and Protest Against Genetically Engineered Corn," described at the beginning of this essay. Hundreds of people marched in streets and chanted slogans, all in the service of claims their organizers know to be lies.

LESSONS LEARNED?

The allegations of DNA contamination of Mexican maize is another example—as if another one was needed—of the use of bio-fraud by radical environmental groups. A highly regarded scientific journal was duped into publishing a letter to the editor containing false data; anti-technology advocates cynically promoted it to the news media, which unwittingly spread the lie to millions of readers and listeners. In mid-April, in the ultimate insult to our intelligence and their own, hundreds of people marched in the streets repeating the lie.

The lessons this time are quite clear. Environmental advocacy groups cannot be trusted to tell the truth. Their alarmist rhetoric damages the scientific process and costs badly needed jobs and export income. Those who would march in the street in support of such lies deserve our pity, not our respect.

FOR MORE INFORMATION...

What Biotech Food Can Do for the Consumer. Most of us are aware of only those technologies with which we, as individuals, have experience. That is no less true of the technologies supporting our food supply. (*Consumers' Research*, January 2002, 4pp.)

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Health Care

Twila Brase

Public health nurse Twila Brase is president of Citizens' Council on Health Care.

"I Thought My Insurance Covered That"

With increasing frequency, the insured are finding themselves in the unhappy shoes of the uninsured. Although they have an insurance policy, an insurance ID number, and proof of premium payments, health coverage is often unavailable without the say-so of the insurer.

Carefully worded exceptions permit health insurers to refuse coverage for services the insured need, treatment they have already received, or procedures that can improve their quality of life. Medical-directors-turned-health-plan-accountants can direct that patient lives be prolonged, improved, jeopardized ... or allowed to fade away.

He who holds the gold makes the rules. He who doesn't pleads, goes to court, dies, or finds another health plan. Patients who make the rules are those who buy an inexpensive major medical health insurance policy and assume financial responsibility for routine and minor health care expenses—with or without a medical savings account.

> *He who holds the gold makes the rules. He who doesn't pleads, goes to court, dies, or finds another health plan.*

The advantage of personal control over health care dollars becomes more evident when citizens discover major gaps in their health coverage. The following ten tips for finding the "uninsurance" in health insurance policies may prove useful to patients and consumers.

1) Request a copy of the entire insurance contract and read it before you purchase the health insurance policy, or choose it from your employer. Simple descriptions and comparison charts will not allow you to understand the limitations of the policy. Your life may someday depend on a well-informed decision.

2) Identify exceptions to the rule before you become sick or injured. Read the fine print, the footnotes, and all exception clauses to health insurance coverage. Exceptions exist in every health insurance policy, but some policies, like those that include medical savings accounts, give policyholders more control over dollars and decisions.

3) Carefully read the criteria for determining medical necessity. Coverage decisions revolve around the insurer's definition of medical necessity. Although the policy covers many procedures and various lengths of stay in health care facilities, the insurer may not consider your procedure or your stay "medically necessary."

4) Know the rules about prior authorization. Some insurers require authorization even in emergencies. Some require it for certain procedures or above certain costs. Failure to get permission for treatment may mean your insurance coverage no longer applies to that episode of care, regardless of the expense.

5) Realize that all staff at a network-approved hospital may not be part of the network. Services provided by a non-network practitioner may allow the insurer to deny payment for the services, even in an emergency.

6) Know the process for appealing a denial of coverage. How many steps are in the process and what is the maximum number of days an insurer may wait to respond at each step? If the process is long, realize you may have to pay out-of-pocket to obtain care while you appeal the decision.

7) Call the network's clinics and doctors before you purchase a policy. The insurer's network may have fewer doctors than the network list indicates. The list may be out-dated, doctors may have left the network, doctors may not be accepting new patients, or doctors may specifically not be accepting Medicaid or Medicare patients. With fewer doctors available, you may have to pay emergency room costs to get timely care.

8) Read rules about access to specialty care. Find out if access requires a referral and if access includes referrals outside the network at no cost or extra cost. Find out how many specialists are available through the insurer's network, and if all specialists listed in the network are still available. If specialists are limited, the wait to see a specialist may jeopardize your health, or require you to go out of the network and pay more.

9) Request a copy of the insurer's drug formulary (list of approved medication). Not all drugs are available in all insurance plans. Ask about the procedure for requesting coverage of a drug not listed on the formulary.

10) Realize you may have to pay more than your deductible to reach your deductible. In traditional indemnity insurance plans, payment toward your deductible is based on the "Usual, Customary and Reasonable" price of a service. Regardless of what you pay for care, only the UCR portion of a payment will apply to the deductible. Therefore, if the UCR of a test is $100, and the cost is $150, only $100 will apply to the deductible even if you paid $150.

For More Information...

Improving Americans' Health Care Coverage Through Defined Contribution. Before voting on any patients' bill of rights, Members of Congress would do well to examine the growing movement toward defined contributions: a new insurance solution that empowers employees by enabling them to choose from among several health plans and to switch plans if they are dissatisfied. (The Heritage Foundation, June 2001, 2pp.)

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Law

End Eminent Domain Abuse

Dana Berliner and Scott Bullock

Dana Berliner and Scott Bullock are both senior attorneys at the Institute for Justice. They currently litigate cases challenging eminent domain abuses in Connecticut, Mississippi, and New York. For more information, visit **www.castlecoalition.org**.

Most people would be shocked to discover that governments across the nation are taking individual's homes, only to transfer that property to a favored business or neighbor. Or that businesses are often being condemned, just so that another business can take the property and make a larger profit.

Yet in the last few years, that's exactly what's been going on. Local governments in particular have taken private homes and businesses to replace them with other privately owned businesses, malls, industrial developments, and upscale housing.

- In **New London, Connecticut**, a private organization has been given the government's power to condemn more than a dozen properties, including the home of an 82-year-old grandmother, for construction of an office park and other development to complement a nearby Pfizer research facility.
- **Merriam, Kansas** condemned one car dealership so that a higher-profit neighboring BMW dealership could expand.
- And in **Riviera Beach, Florida**, the city is moving forward with plans to force out more than 5,000 residents for privately owned commercial and industrial development.

These are a few of the situations described in a report issued recently by the newly formed Castle Coalition, "Government Theft: The Top Ten Abuses of Eminent Domain, 1998-2002." Selected from more than 100 such abuses around the country, the report describes 10 of the most egregious examples of government taking homes or businesses from their rightful owners to transfer the land to a more politically or financially powerful private party. Although both federal and state constitutions forbid takings for private use, government agencies at all levels ignore this prohibition.

ACTIVISM CAN HELP

Court battles to protect against such abuse are long, arduous, and often prohibitively expensive, particularly when the cost is borne by one or two property owners. As lawyers at a nonprofit organization, we cannot handle even a tenth of the abusive eminent domain cases that come to our attention. But local and national activism can dramatically change the landscape, scuttling attempts by government to help private parties steal property for pet projects.

Over the past several years, we have seen rising popular indignation and resistance against this abuse of eminent domain. Property owners and activists have become increasingly vocal and increasingly successful in their opposition. Home and business owners in **New Rochelle, New York** defeated a plan to replace their neighborhood with a new IKEA store. An organized community in **Baltimore County** allowed citizens to vote on a referendum that overturned a plan to condemn a large area for commercial and industrial development.

The opponents of eminent domain abuse have experimented with an enormous range of strategies. They've circulated petitions, sponsored successful voter referenda, picketed the Swedish consulate, erected billboards, talked to their neighbors, and talked to people they never in a million years thought they'd find common ground with.

UNITED WE STAND

Across the country, there once were isolated pockets of dedicated activists fighting to defeat plans to raze their homes and businesses for the benefit of private parties. Now, they are uniting.

The new network is called the Castle Coalition, because everyone's home, and everyone's property, is their castle—a place where they should be safe and free from government overreaching. Homeowners, civil rights activists, and small business owners from 15 states have united to trade strategies and learn how to effectively fight eminent domain abuse in their communities.

Under the U.S. Constitution, our property rights are not conditioned on the whim of those with financial and political influence. Nor should they be sacrificed just so municipalities can put more money in their coffers.

If an elderly widow's house in Des Plaines, Illinois can be condemned for a Walgreens, no one's home is safe. Under the U.S. Constitution, our property rights are not conditioned on the whim of those with financial and political influence. Nor should they be sacrificed just so municipalities can put more money in their coffers.

It's time for citizens to tell their state and local governments that enough is enough. The abuse of eminent domain to take property for other private parties must end. That's what the Castle Coalition intends to accomplish.

FOR MORE INFORMATION...

Government Theft: The Top 10 Abuses of Eminent Domain: 1998-2002.
"Eminent domain ... is a despotic power ... Yet government increasingly uses the eminent domain power to condemn property for private uses. Acting more like real estate agents than public servants, government agencies form unholy alliances with developers in order to force the rightful owners off of their property." (Castle Coalition, 2002, 14pp.)

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Privatization

L. Lynne Kiesling

L. Lynne Kiesling is director of economic policy and director of privatization research at Reason Public Policy Institute, and senior lecturer of economics at Northwestern University.

Technology Enables Government Accountability

As government has evolved, particularly in the past century, government budgeting processes and outcomes have become increasingly separated from program or project objectives. Program planning that focuses on budgets—particularly for programs whose budgets have built-in "use it or lose it" incentives—may not achieve the program's goals, let alone do so in a cost-effective manner.

Measures of government activity tend to focus on budgets and how much they increase each year. That focus has fostered an agency-centric model of government that requires citizens to serve the needs of agencies, rather than vice versa. Citizens stand in line, fill out forms, and eventually achieve their objective only after investing substantial time and effort in the process. The red tape and paperwork can leave citizens feeling dissatisfied and at a loss as to how they can interact with their government more effectively.

Making budgets more transparent, and connecting them to actual program performance, could improve the cost-effectiveness of government programs and ease citizens' frustration with the quality of government services.

Making budgets more transparent, and connecting them to actual program performance, could improve the cost-effectiveness of government programs.

MEASURING PERFORMANCE

Geoff Segal and Adam Summers at Reason Public Policy Institute have written a "how to" guide for governments striving to improve performance, accountability, and cost-effectiveness of government services.

Citizens' Budget Reports: Improving Performance and Accountability in Government offers specific recommendations to help government officials think more strategically and tie budgets to performance, improving cost-effectiveness and citizen/taxpayer satisfaction.

Segal and Summers identify six dimensions of service outcomes to evaluate: quality, efficiency, timeliness, accuracy, accessibility, and professionalism. By using those dimensions as a guide, governments can work backward from desired outcomes to the activities that will best achieve them.

Some of the performance measures Segal and Summers suggest are traditional input indicators. While input measures help government officials and citizens assess the value their efforts are creating, relying solely on such measures is likely to produce a backslide into the type of input-based budgeting that has contributed to the poor quality public services and lack of civic engagement we see today.

For that reason, performance should also be measured by output indicators, intermediate outcomes, and effectiveness indicators. By incorporating strategic planning into the budgeting process, governments can identify such indicators, implement processes to measure and evaluate them, and feed the information back to citizens, employees, and program administrators.

ROLE OF TECHNOLOGY

Measuring performance in the provision of government services is not a new idea. But only recently has interest grown in actually *implementing* performance measurement. That interest has been spurred by changes in technology that make collecting performance data easier, less time-consuming, and less costly.

Many government agencies are implementing electronic service provision, getting people "online and out of line" through e-government initiatives. Information technology can make it easier for citizens to hold their governments accountable by providing better information about the inputs, outputs, intermediate outcomes, and effectiveness of government service provision. Online surveys and comment opportunities can generate important effectiveness information for program and project administrators.

Technology and e-government have also made governments rethink how they interact with their citizens. As e-government services have evolved, the consensus seems to be in the direction of citizen-centric, rather than agency-centric, models.

The type of performance measurement Segal and Summers describe takes the idea of the technology-enabled citizen even further. By coupling the citizen-centric service model with input, ouput, intermediate outcome, and effectiveness measures, the process will generate more civic engagement, more accountability, better quality control and professionalism, and improved policy discussions through the informed examination of alternatives.

BETTER GOVERNMENT ... OR SMALLER?

What are the likely consequences of making government more accountable and efficient? Will making government better be counterproductive for those who want to see it *smaller*?

Focusing on performance shifts the debate from intentions to results. Transparency and accountability can be strong tools for eliminating programs that do not deliver, or for privatizing or outsourcing them. More accountable government and limited government are complementary goals ... and both are served well by performance measurement and budgeting processes.

FOR MORE INFORMATION...

Citizens' Budget Reports: Improving Performance and Accountability in Government. "To improve the relationship between the governed and the governing, governments need to focus on better performance, more efficient government, and an informed citizenry. ... To properly serve their citizens, governments need to make data available so that policymakers and citizens fully understand the array of results that can be accomplished through different levels of spending." (Reason Public Policy Institute, March 2002, 48pp.)

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Regulation after September 11

Susan E. Dudley

Susan E. Dudley directs the Public Interest Comment and Regulatory Accounting projects of the Regulatory Studies Program of the Mercatus Center at George Mason University.

Since the terrorist attacks last September, Americans' support for government has increased as they come together in the face of outside threats.

A poll conducted by Gallup a few days before the attacks asked whether the government is trying to do too many things that should be left to individuals and businesses, or whether it should do more to solve the country's problems. Fifty-five percent thought the government was doing too much, while 36 percent thought it should do more.

When the same poll was repeated after the attacks, the results flipped; only 41 percent believed the government was doing too much, while 51 percent felt it should do more.

As Robert Higgs documented in his 1987 book, *Crisis and Leviathan*, federal expenditures increase during periods of national crisis ... but then never fully recede to their pre-crisis levels. Periods of crisis tend to create a feeling among citizens that extensions of government power are legitimate and necessary to maintain order and economic stability. That leads to a more permanent reliance on government and an erosion of individual responsibility and freedom.

President Woodrow Wilson first introduced the income tax as we know it while the nation was preparing for World War I. During World War II, income tax rates increased, and automatic paycheck deduction was implemented. That wartime tax collection vehicle remained after the conclusion of the war.

REGULATORY RATCHET

This ratchet effect also is evident in regulatory activity. The number of pages in the *Federal Register*, which has served as a daily compendium of federal rules and notices since 1936, increases by 20 percent on average during national crises (including wars and the "moral equivalent of war," such as the 1970s energy crisis). Growth in the number of pages appears to continue on a steeper path after the crisis ends.

History suggests we are more likely to see economic rather than social regulations during periods of war. During both World Wars, for example, the federal government took over factories and railroads to secure supplies for defense efforts. Most of these confiscated resources were returned to private hands at the conclusion of hostilities, but with residual regulatory controls that hadn't existed before the war. The railroads were returned to their owners in 1920, but the powers of the Interstate Commerce Commission were expanded to include complete control over rates, securities offerings, mergers, and construction, as well as use and abandonment of rail facilities.

Since September 11, airport security is the most visible case of the federal government taking over a private activity. The November 2001 aviation security legislation puts federal employees in charge of airport security screening for at least the next three years. Like the resources commandeered during previous wars, airport security operations may be returned to private hands after three years, but only at the request of individual airports, and only with increased federal scrutiny.

Unlike economic regulations, "social regulations" are generally intended to promote environmental quality, or the health and safety of consumers and workers. The greatest increases in social regulations historically have occurred during times of peace and prosperity, rather than in response to crises. The sharpest increase in social regulatory activity occurred during the post-Vietnam period of the 1970s.

WILL HISTORY REPEAT ITSELF?

America is at a pivotal point in its history. We have witnessed a major shift in our national priorities. Environmental and other domestic social issues have taken a back seat to national security matters. The government has enacted, with little dissent, federal laws the public would not have tolerated before September 11. For example, the USA Patriot Act, signed into law on October 26, includes money-laundering provisions very similar to a "know-your-customer" proposal the Federal Deposit Insurance Corporation withdrew two years ago in the wake of unprecedented negative public comment.

From our country's founding, Americans have been skeptical of government. It remains to be seen whether that skepticism can be preserved through these troubled times.

From our country's founding, Americans have been skeptical of government. It remains to be seen whether that skepticism can be preserved through these troubled times. As the threat from terrorism fades, elected officials may feel pressure to take a major role in domestic as well as national defense issues. If historical patterns hold true, we may see a further erosion of our individual freedoms as the federal government moves beyond its unique and essential role in national defense, toward greater federal regulation of private activities.

FOR MORE INFORMATION...

Combating Terrorism, Protecting Freedom. Malcolm Wallop (former U.S. senator), David Kopel (Independence Institute), and Nadine Strossen (ACLU) were among the speakers at a fall 1996 Cato Institute conference addressing terrorism in the modern world. (Cato Institute, 1996, 3pp.)

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Taxes

Bill Ahern

Bill Ahern is communications director of the Tax Foundation.

Tax Freedom Day® Finally Arrives

America celebrated Tax Freedom Day® on April 27, 2002—two days earlier than in 2001, and four days earlier than in 2000.

At an April 10 news conference at the National Press Club, Tax Foundation Executive Director Scott Hodge announced the findings of a new Tax Foundation report on the nation's tax burden. Tax Freedom Day® is the nation's most popular barometer of the average American's total tax burden.

In the report—*Tax Foundation Special Report No.* 112, "America Celebrates Tax Freedom Day®"—economists Scott Moody and David Hoffman explain why the overall tax burden has been trending down the last two years, pushing Tax Freedom Day® back into April, after a long string of later and later Tax Freedom Days.

"Two factors are combining to make the average American's tax burden lighter in 2002," said Moody, "federal tax reductions in 2001 and 2002 and a slower economy."

TAXES AND OTHER EXPENSES

The number of days the average American must work to pay taxes can be compared to the price of other important categories of consumer spending. Americans will work longer to pay for government (117 days) than they will for food, clothing, and shelter combined (106 days).

Only in the last decade have taxes exceeded spending on these basic necessities, and federal taxes alone cost Americans more (80 days) than any other major budget item.

TAX FREEDOM DAY® BY STATE

Tax burdens vary considerably from state to state, not only because of different state and local taxes, but also because the citizens of each state pay dissimilar federal taxes. Connecticut has the heaviest total tax burden and so celebrates Tax Freedom Day® the latest—on May 14. Alaskans pay the least and are finished working to pay taxes on April 8. (See table.)

COMPARING STATE/LOCAL TAX BURDENS

To facilitate comparisons of state/local tax burdens, the new Tax Freedom Day® report also presents each state's tax burden with federal taxes excluded for the last decade. The nation's average state/local tax burden is 10.2 percent of residents' income, with the highest being Maine's 12.8 percent and the lowest being Alaska's 6.3 percent.

The Tax Foundation is a nonpartisan, nonprofit organization that has monitored fiscal policy at the federal, state, and local levels since 1937.

TAX FREEDOM DAY® BY STATE AND RANK 2001 AND 2002

State	2001 Tax Freedom Day®	2002 Tax Freedom Day®	Rank in 2002
U.S.	April 29	April 27	-
District of Columbia	May 17	May 17	-
Connecticut	May 17	May 14	1
Washington	May 12	May 09	2
New York	May 09	May 06	3
New Jersey	May 08	May 05	4
Wyoming	May 06	May 04	5
Wisconsin	May 03	May 01	6
Minnesota	May 01	April 29	7
Michigan	May 02	April 29	8
Illinois	May 02	April 29	9
California	May 02	April 29	10
Maine	April 30	April 29	11
Massachusetts	May 02	April 28	12
Rhode Island	April 30	April 28	13
Nevada	May 01	April 27	14
Florida	April 30	April 27	15
Vermont	April 30	April 27	16
Delaware	April 28	April 25	17
Arizona	April 28	April 25	18
Nebraska	April 28	April 25	19
Ohio	April 27	April 25	20
New Hampshire	April 29	April 25	21
Georgia	April 27	April 24	22
Kansas	April 27	April 24	23
Colorado	April 27	April 24	24
Virginia	April 26	April 24	25
Arkansas	April 25	April 24	26
Utah	April 26	April 23	27
Pennsylvania	April 26	April 23	28
Maryland	April 26	April 23	29
Hawaii	April 25	April 22	30
Indiana	April 25	April 22	31
Iowa	April 24	April 21	32
Oregon	April 24	April 21	33
New Mexico	April 23	April 21	34
North Carolina	April 22	April 20	35
Texas	April 24	April 20	36
Idaho	April 23	April 20	37
Missouri	April 22	April 20	38
Kentucky	April 22	April 20	39
South Carolina	April 22	April 20	40
Louisiana	April 21	April 19	41
Montana	April 20	April 18	42
Mississippi	April 20	April 18	43
South Dakota	April 21	April 18	44
North Dakota	April 19	April 17	45
Tennessee	April 19	April 16	46
Alabama	April 18	April 16	47
West Virginia	April 17	April 16	48
Oklahoma	April 17	April 15	49
Alaska	April 11	April 08	50

FOR MORE INFORMATION...

America Celebrates Tax Freedom Day®. The full text of the 2002 Tax Freedom Day report includes state-by-state analysis. How does *your* state rank ... and why? (Tax Foundation, April 2002, 12pp.)

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Software Industry Battles the Regulators

Bartlett D. Cleland

Bartlett Cleland is director of the IPI Center for Technology Freedom. Formerly he served as technology and policy counsel for Americans for Tax Reform, and earlier he was counsel to Senator John Ashcroft.

The software industry is, once again, under attack from a handful of vocal, influential people. This time around, the vociferous critics claim flaws in software products allow criminals to exploit the software to their own ends.

While the rhetoric makes for good headlines, it tells only part of the story. Unfortunately, some members of Congress are buying into the rhetoric, and Congressional hearings will be held in the next month or two on alleged software vulnerabilities. The result could be catastrophic for one of the country's most innovative and successful industries: Software companies could face regulation by the federal government, even legal liability if they do not produce flawless products.

The National Academy of Sciences has been one of the loudest critics of the industry. According to *CIO Magazine*, a panel of Academy representatives believes: "Congress should make it easier to punish companies that produce insecure software that puts business and consumers at risk." Perhaps even more worrisome is the push by the Air Force's chief information officer to establish a set of government standards to regulate the software industry.

> *Consumers and producers would lose; only the trial lawyers would win, lining their pockets with the rewards of subdued innovation.*

WON'T SOLVE THE PROBLEM

Most of the critics can point to only a few products from a couple of companies when making these remarks. Their comments, however, are aimed at a much broader agenda: to regulate the software industry.

But regulation, whether through legislation or litigation, won't solve the problem, because it doesn't address the real cause of security weaknesses. Worse, regulation *will* result in the loss of current benefits that software provides, and it will stifle the innovation necessary to produce better software in the future.

One of the biggest kinks in software security and operability is the user. All too often, consumers do not install or use software correctly. Law enforcement officials are routinely able to defeat even the most robust encryption software because of faulty installation or application by the user. There's no need for law enforcement officials to take on the software directly (the "brute force" approach): They needn't break down the software door, as it were, because users have left it open.

In the same way, criminals take advantage of user implementation "holes," rather than searching for software development "holes." This is a security issue that defies litigation or legislation.

STIFLING INNOVATION

Software development is a complex process conducted in a rapidly changing business and technical environment. A government-designed regulatory review and approval process simply could not keep pace with the changes.

Regulation-by-litigation would be as bad. Fearing lawsuits unless their programming was "perfect," software companies would stop producing new products. Only the largest would have pockets deep enough to risk new inventions. Consumers and producers would lose; only the trial lawyers would win, lining their pockets with the rewards of subdued innovation.

The ubiquity of computing has rapidly expanded the base of users—exposing, and sometimes causing, problems that were not problems when the user base was smaller and more sophisticated. Government agencies are not immune to these user issues. Indeed, they may be the last groups you'd want to trust with setting software standards and establishing rules for user implementation.

A Defense Department inspector general's report recently concluded the Air Force is posting security-sensitive information on many of its Web sites. The report showed the Air Force had 140 publicly accessible Web sites with "potentially inappropriate" information. Those sites displayed warnings such as "For Official Use Only" and "Secret" ... yet they were all accessible by the public. Moreover, the report found the Air Force—like civilian software users everywhere—had a process that "was not reliable" for removing sensitive data.

TRUST THE MARKET

Software provides untold benefits, but it is not and never can be infallible. No one recognizes this better than the industry itself. The software industry is continually—and successfully—working to improve the quality, usability, and security of its products. This constant innovation, driven by the competitive marketplace, is what's best for consumers and all citizens.

Regulation, by legislation or by litigation, would bring this natural evolutionary process to a grinding halt. The idea of money brought in by lawsuits or settlements may be appealing. Ham-handed federal government intervention may seem an instant panacea on the homeland security front. But these are not lasting solutions. Regulation of the IT industry, or of its software component, only mortgages the future of our economy ... and our security.

FOR MORE INFORMATION...

SIIA Comments on Consumer Protection in the Global Electronic Marketplace. Position paper issued by the Software & Information Industry Association, outlining its case for limited government intervention into e-commerce, the Internet, and other industry matters best addressed by consumers making decisions in a free, competitive marketplace. (Software & Information Industry Association, March 26, 1999, 3pp.)

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Welfare

Jennifer Garrett

Guest columnist Jennifer Garrett is a researcher in domestic policy studies for The Heritage Foundation, a Washington-based public policy research institute.

Marriage Reduces Poverty

The Alternatives to Marriage Project (ATMP) and several women's groups oppose President George W. Bush's plan to include marriage promotion in welfare reauthorization, claiming marriage-promoting policies harm more children and families than they help.

Their newly released report, "Let Them Eat Wedding Rings: The Role of Marriage Promotion in Welfare Reform," comments on the misguided attempts to end poverty by using welfare dollars to promote marriage. The report falsely concludes marriage is not an effective solution to poverty, and that there is no clear relationship between marriage rates and child poverty.

In fact, however, studies show that the fastest way to escape poverty is to get married ... and the fastest way into poverty is divorce. The reason: Two incomes are better than one. Or, in the case where a spouse is unemployed, one income is better than none.

A child born and raised outside of marriage will spend 51 percent of his childhood in poverty. By contrast, a child born inside marriage and raised by both parents in an intact marriage will spend only 7 percent of his childhood in poverty. A child raised by a never-married mother is more than seven times more likely to be poor than a child raised in an intact marriage. Children who grow up with absent fathers are also more likely to drop out of school, become addicted to drugs, have a child out-of-wedlock, or end up in prison.

Instead of embracing these findings, women's groups such as the ATMP choose to repudiate them, in an attempt to preserve their own "marriage to the government."

DISCRIMINATION IN WELFARE

The report further suggests welfare policies should not discriminate on the basis of marital status. In reality, the welfare system already discriminates ... against married-couple families. Welfare programs penalize single mothers who choose to free themselves from the cycle of dependency and marry. Welfare penalizes marriage and rewards single parenthood because of the inherent design of all means-tested programs.

In a means-tested program, the benefits are reduced as non-welfare income rises. Thus, under any means-tested system, a mother will receive greater benefits if she remains single than if she is married to a working husband. Welfare not only serves as a substitute for a husband, it actually penalizes marriage because a low-income couple will experience a significant drop in combined income if they marry. In order to encourage marriage, welfare policies should not discriminate against married couple families, the type of household most beneficial to children.

HEALTHY MARRIAGES SHOULD BE THE GOAL

These studies illustrate the importance of encouraging healthy marriages and two-parent married families as a major goal of welfare reform. That's why the President's plan directs up to $300 million in block grants to states for programs that encourage healthy, stable marriages. These programs include pre-marital education and counseling, as well as research and technical assistance into promising approaches that work.

Too many Americans have been injured by the helping hand of the state. The welfare system has become the enemy of individual effort and responsibility, with dependence passed from one generation to the next.

Overall welfare caseloads increased substantially over the last 30 years. Between 1965 and 1995, federal and state spending on the poor increased from around $40 billion to more than $350 billion a year. Yet, during the same 30-year period, we've made virtually no progress in reducing child poverty.

> *[M]ost women don't want to be married to the government. They want to be free to make their own decisions, choose their own destiny, and make their children's lives better ... without government interference.*

It's time to try something else ... to change a system that rewards failure and punishes success; that encourages dependency and illegitimacy, and discourages marriage and work.

Many welfare recipients will concur. In fact, the majority of former welfare families feel it is more rewarding to be a responsible citizen than a welfare client; it is better to be a breadwinner respected by your family.

And, despite what ATMP believes, most women don't want to be married to the government. They want to be free to make their own decisions, choose their own destiny, and make their children's lives better—without government interference. Raising children by themselves is an incredibly difficult job. In many cases, their lives and their children's lives would be better if they and the fathers of their children were united in marriage. The government is no substitute for a spouse.

Welfare reform's priorities should be the reduction of dependency and poverty through work and marriage. We must face the impact of deteriorating marriage forthrightly. There is no better time to start than now.

FOR MORE INFORMATION...

The Coming Crisis: How Government Dependency Threatens America's Freedom. When the majority of citizens get government checks and the rest of us have to pay for them, freedom is under siege. Government dependency threatens us all. Congressman Jim DeMint offers an obvious but painful solution. (The Heritage Foundation, May 2001, 9pp).

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Term Limits: An Idea Built on Solid Ground

by Stacie Rumenap

Maybe what the career politicians need is a silver cross.

The term limits movement is so persistently popular it has already been given about a million obituaries. Of course, when something is really dead, you need to pronounce the last rites only once.

As term limits began triumphing around the country in the early 1990s, one of the first obits was delivered by Speaker of the House Tom Foley (D-Washington)—right after voters in 14 states term-limited their congressional delegations and statehouses.

The Speaker was so annoyed he sued his own Washington State constituents to overturn the limits. Voters were so annoyed they handed him a stunning defeat in the very next election—rewarding a virtual unknown who had pledged that he, for one, would serve only three terms in Congress. (A mere campaign ploy, as it turned out; Foley's opponent would soon unveil himself as Just Another Career Politician.) The movement that was already "running out of steam" had just ejected a sitting Speaker of the House.

LAME ARGUMENTS

If obituaries can't kill term limits, maybe arguments will. But the critics keep coming up with such lame ones.

"We already have term limits. They're called elections." (As if a rigged field is a fair field.)

"If you have term limits, all the power will go to the lobbyists and bureaucrats." (Who oppose term limits by the same overwhelming margins the career politicians do, even in the term-limited states where they're allegedly being handed all this power.)

"The new guys are too inexperienced to find the bathroom." (Are there no maps?)

> *[M]ost of the public like term limits just fine. It may not be at the top of their "most-important-issue" list. But whenever they get a chance to vote for term limits, they do.*

The latest version of all this is Michael Flynn's "Term Limits: An Idea Built on Sand," which ran in the November/December 2001 issue of *Intellectual Ammunition*.

Flynn claims the high reelection rate for congressional incumbents is not really evidence of incumbent advantage. Thanks to gerrymandering (politically motivated line-drawing of districts), according to Flynn, "a large number of legislative districts are simply not competitive."

But isn't it usually the *incumbents* who get to draw those lines? Sounds like an advantage of incumbency to us!

Flynn also avers that to be fair in measuring incumbency advantage, you've got to compare only those races in which the incumbent and challenger are already spending comparable amounts of money. But numbers don't tell the story all by themselves; you've got to consider them in context. Incumbents don't have to spend very much money at all if they have no significant opposition in an election.

Eric O'Keefe, president of Americans for Limited Terms, points out that if Flynn were to study congressional election returns a little more closely, he'd see that in 1998 (the latest election year for which we have detailed figures), "the reelection rate of incumbents who spent under $600,000 was 100 percent. Almost all the defeats came from those who spent over $1,000,000. High spending often indicated a serious challenge, therefore vulnerability.

"Another thing Flynn ignores is the partisan composition of districts," O'Keefe adds. "Most state legislative districts are never competitive in a general election, even when there are open seats. Those with roughly equal spending are among the small minority that are not one-party, where the bulk of inter-party fighting occurs. They get well funded by the parties because they are competitive. Flynn has cause and effect backwards."

GIVE THE PEOPLE A CHANCE

Sure, the term limits movement is embattled. Career politicians don't like the idea of a periodic stimulus to electoral competition. Advantages of incumbency that result in mere token (or even zero) electoral opposition in a district are just fine with them.

A rigged game ... permanent power ... only the special interests to answer to ... everybody saying "yes sir" and rushing to hold open the door ..."fact-finding" junkets to Bermuda ... what's not to like? It's only the public at large and other such partisans of democracy that could see any problem.

It's equally obvious why most of the public like term limits just fine. It may not be at the top of their "most-important-issue" list. But whenever they get a chance to vote for term limits, they do.

Judging by what the people do when the people have a chance, term limits is the most successful political movement of our time. The term limits movement will prevail. In this country, friends of democracy far outnumber the friends of oligarchy. And the battle is just beginning. Mr. Flynn, join us.

❖

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Taxes and Economic Growth: A Strategy for State Officials

study by Dr. Richard Vedder
excerpt by Teresa Bauman

In September 2001, Taxpayers Network, Inc. released *Taxes and Economic Growth*, a 28-page report by Professor Richard Vedder of Ohio University. The report asks, and answers, the question, "Should states adopt a safe haven strategy of low tax burdens to foster economic growth, capital formation, and innovation?" The report is summarized in the article below, written by Teresa Bauman, a freelance writer.

A free copy of the complete report may be obtained by e-mailing your name and mailing address to mriley@taxpayersnetwork.org. Or use the Web-based order form at **http://www.taxpayersnetwork.org/taxeseconomicgro.html**.

* *

As state legislatures grapple with how to balance their budgets, a new report suggests spending cuts be generous and income taxes—for decades a bottomless source of revenue for the perpetual expansion of state government—be thrown out and replaced with the sales tax.

The report, authored by Ohio University economist Richard Vedder, offers more resounding evidence that the income tax, more than any other form of taxation, has a detrimental effect on economic growth and Americans' overall financial well-being.

"The income tax is the champion of bad taxes, in terms of its destructive effect on people, prosperity, and their economic well-being," according to Vedder.

To demonstrate the negative effect of income taxes on economic opportunity, the study takes a 40-year look at the personal incomes of citizens living in high- and low-tax states. The results show that the lower a state's tax burden, the higher the rate of personal income growth for its citizens. Figure 1 shows that between 1957 and 1997, real personal income growth was more than twice as high in the states that did not raise their income taxes (or increased them only minimally), compared to states with the biggest increases in income taxes.

The report also uses state comparisons to illustrate the impact of taxes on economic growth. For example, while Kentucky and Tennessee are alike in many respects, these neighboring states have contrasting economies because they have taken different fiscal paths over the past 40 years. While Kentucky implemented massive hikes in its income tax between 1957 and 1999, Tennessee never even adopted an income tax. As a result, by 1997, Kentucky's overall tax burden was 25 percent higher than Tennessee's. On average, a family of four in Tennessee earned $703 more per month than its counterpart in Kentucky.

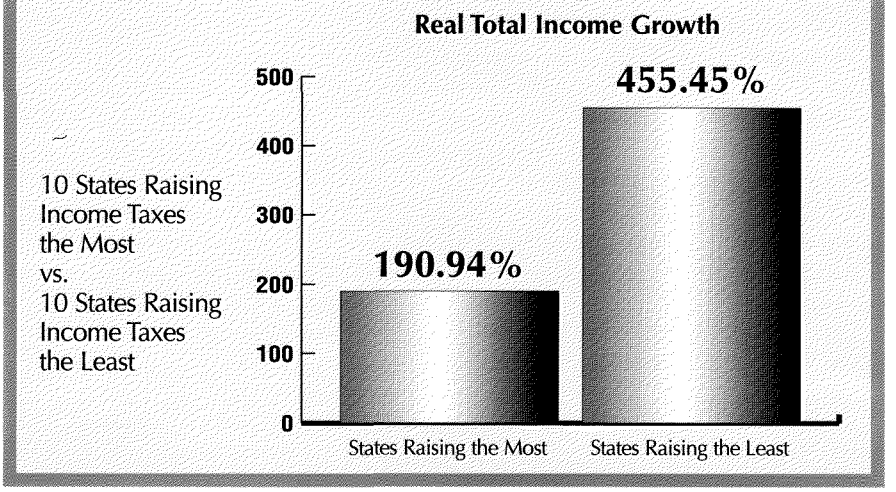
SALES TAX VS. INCOME TAX

As most states in the nation struggle to dig their way out of large budget deficits, Vedder encourages policy makers to "avoid the enormous temptation to raise taxes." Instead, he suggests they cut spending and then reverse their dependence on the income tax by turning to a sales tax approach for funding essential services.

> *The income tax is the worst of taxes. It's a tax on labor, on production, on what people contribute to society.*

Vedder criticizes the income tax as a punitive levy on people's positive and productive activities. "The income tax is the worst of taxes. It's a tax on labor, on production, on what people contribute to society," he said.

Figure 1
ECONOMIC PERFORMANCE



Source: U.S. Department of Commerce, Vedder calculations

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Property taxes also have an adverse effect on economic growth, Vedder concludes. Just as in the case of income taxes, states with high property taxes experienced less personal income growth when compared to states with low property taxes.

So when it comes to taxes, Vedder believes his research clearly shows the sales tax is the tax of choice. It is a less harmful approach for raising revenue, he said, because "it does not tax production, but rather what people consume, what they take away from society."

VOTING WITH YOUR FEET

"Let's pack up and move!" Taxpayers aren't just saying it—they're doing it. *Rather than paying income taxes, people are moving to destinations that* allow them to keep more of their hard-earned money.

"It's no secret why Bill Gates, the richest man in the world, lives in the state of Washington," said Vedder, noting Washington does not have an income tax.

Vedder's report, which tracks the movement between 1990 and 1999 of native-born Americans within the United States, showed that nearly 3 million people moved *out of* states that impose an income tax *and into* states without an income tax: Alaska, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington, and Wyoming.

"With the exception of Sundays, some one thousand persons moved every day for nine years to the no-income-tax states," Vedder reported.

HOW DO THE STATES STACK UP?

According to the report, income taxes are such potent revenue sources—with revenues typically rising faster than personal income—that they provide governments with great revenue growth.

*However, because politicians tend to spend and not save added rev*enue, income tax states are generally big-government states, as Connecticut, Delaware, Maine, Minnesota, and Wisconsin show. States likes Florida, New Hampshire, and Texas, which do not have an income tax, also tend to have more moderate levels of government spending and taxation relative to income levels, the report indicates.

Figure 2 shows that between 1957 and 1997, the average overall tax burden rose by 37.2 percent in the states that adopted new income taxes, compared with a more moderate 10.5 percent increase in the no income tax states.

According to Vedder, states wishing to increase economic opportunity for their citizens must have a low overall tax burden. Also, they must rely mainly on consumption or sales tax-based taxes more than those that impact production, such as income and property taxes.

The report uses these criteria to rank and grade states according to their overall tax burden. South Dakota, Tennessee, and Texas ranked highest and were awarded A's for having the lowest overall tax burden. None of the three has an income tax. Florida and Nevada, which also do not have an income tax, received an A-.

On the flip-side, Connecticut, Delaware, Maine, Minnesota, and *Wisconsin all received an F for having overall high tax burdens.*

GRADING THE STATES

Do tax policies promote economic prosperity for their citizens?

Grade A	Grade F
South Dakota	Connecticut
Tennessee	Delaware
Texas	Maine
	Minnesota
	Wisconsin

OKLAHOMA MAY GIVE IT A TRY

While some policy makers may think abolishing their state income tax is too radical, at least one state is considering it.

Oklahoma Governor Frank Keating is attracting national attention for his proposal to eliminate the state's individual income tax and raise the state sales tax from 4.5 to 5.9 percent. The Governor's office estimates middle-income families would save $100 to $150 each month under the tax plan.

"Governor Keating is showing the nation that even though ending the income tax is a huge undertaking, it is possible," Vedder said.

It remains to be seen if other states will follow Oklahoma's lead. Regardless of how states address their budget woes, Vedder has three words for those that are thinking about raising taxes: Don't do it.

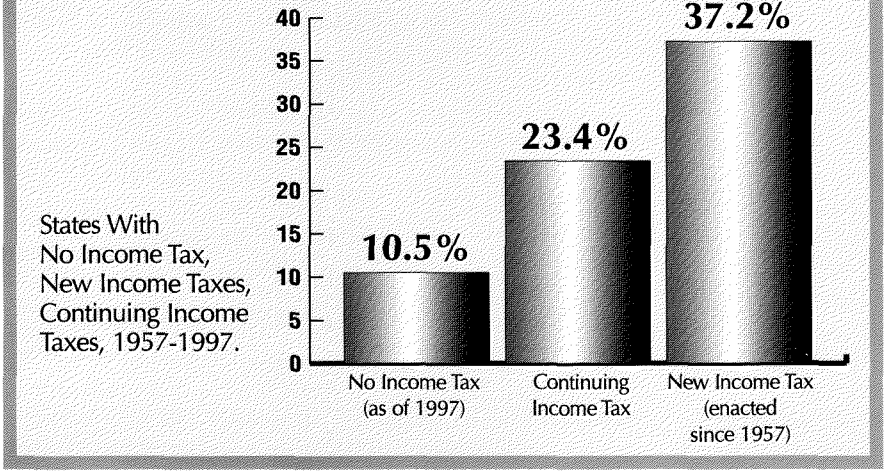
"They should cut government spending. They should also let private industry compete for operating state-run programs, such as university dormitories, prisons, public school transportation and cafeteria services, and highway maintenance," Vedder concluded. "What they should not do, however, is raise taxes."

❖

For more information about Taxpayers Network, Inc., write to TNI, W67 N222 Evergreen Blvd. #202, Cedarburg, WI 53012.

Figure 2

PERCENT INCREASE IN OVERALL TAX BURDEN



Source: U.S. Department of Commerce, Vedder calculations

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It's Not About Microsoft Anymore

by Joseph L. Bast

U.S. District Judge Colleen Kollar-Kotelly is pondering whether to accept a proposed settlement of the antitrust case against Microsoft. She would do well to consider whether the real culprit still on trial is not Microsoft, but the country's archaic and perverse antitrust laws.

Back in 1998, when Netscape, AOL (now AOL Time Warner), Oracle, Novell, and Sun Microsystems were losing market share and profits to Microsoft, they did not redouble their efforts or imitate the successful company's techniques. Instead, they lobbied the U.S. Department of Justice and 20 state attorneys general to sue Microsoft for violating the country's century-old antitrust laws.

A trial court eventually found Microsoft guilty and proposed breaking the company into two entities, one limited to the Windows operating system, the other to applications. On appeal, that remedy was thrown out for being extreme and unrelated to the misconduct at issue.

The settlement now under consideration would prohibit Microsoft from engaging in business practices the trial court found to be anti-competitive. The proposal satisfies Microsoft, the Department of Justice, and 41 of the 50 states. But it doesn't satisfy Microsoft's rivals, who have persuaded nine state attorneys general to oppose the settlement and call for greater restrictions.

There is something profoundly wrong with a system that allows nine publicity-seeking politicians and a handful of rival businesses to determine how a successful company goes about its business ...

ANTITRUST ITSELF IS THE PROBLEM

There is something profoundly wrong with a system that allows nine publicity-seeking politicians and a handful of rival businesses to determine how a successful company goes about its business, and it doesn't take a detective to find the source of the problem. It lies in the antitrust laws themselves. These laws—principally the Sherman Antitrust Act of 1890—were passed to protect politically powerful high-cost producers from more technologically advanced competitors.

The history of the Sherman Act is quite clear: Farmers and ranchers in the Midwest faced falling prices for their products, and they blamed the centralized food and meat processors in Chicago. By breaking up the companies that had achieved the greatest economies of scale, they hoped to return to an era of higher prices and higher profits. The Act wasn't passed by Congress to protect consumers or "the public interest." It was passed to protect political insiders by shackling competitors who were "too successful" at meeting the public's demands.

The Sherman Act punishes companies for failing to do what regulators (typically lawyers) think or claim is in the public's best interest. Under antitrust law, government confiscates the assets of one company for redistribution to its competitors in the name of benefitting consumers. But consumers have no right to a company's private assets, and regulators have no special insight into what is best for consumers. This is just plain bad law.

RETROACTIVE, ARBITRARY LAW

Antitrust laws apply retroactively to conduct that was legal at the time it occurred. Conduct that would be legal for a non-monopolist, such as offering special discounts to vendors in exchange for promotional consideration, is illegal for a monopolist. Since the finding that a company is a monopolist is often made after the fact (in Microsoft's case, some five years after the alleged fact), antitrust law is a species of unjust *ex post facto* law, which the founding fathers wisely forbade in Article I, Section 10 of the Constitution.

Antitrust law is enforced arbitrarily. Historically, antitrust suits have been filed against industries that have been lowering prices and increasing output—just the opposite of what monopolists are thought to do. Most complaints are filed not by public interest groups, but by the less-efficient competitors of industry-leading companies.

Sen. Orrin Hatch (R-Utah), the ranking Republican on the Senate Judiciary Committee, was a high-profile supporter of the Microsoft lawsuit since the very beginning. Utah Attorney General Mark Shurleff, also a Republican, is one of the nine who oppose the proposed settlement. It is no coincidence that Utah is home to Novell, one of Microsoft's rivals. Kenneth Olafson, a member of that state's Republican Central Committee, recently described the views of the Senator's office staff to the *National Journal*: "We're protecting Novell and that's it, we don't care about the facts or what the economy does."

Antitrust law was bad law when it was adopted in the horse-and-buggy days of 1890. It is unconscionably bad law today, in an era of rapid technological change, escalating competition, and widening consumer choices. Judge Kollar-Kotelly ought to approve the proposed settlement and either denounce the perverse and illegal provisions of the Sherman Act or call on Congress to repeal it forthwith. Justice requires no less.

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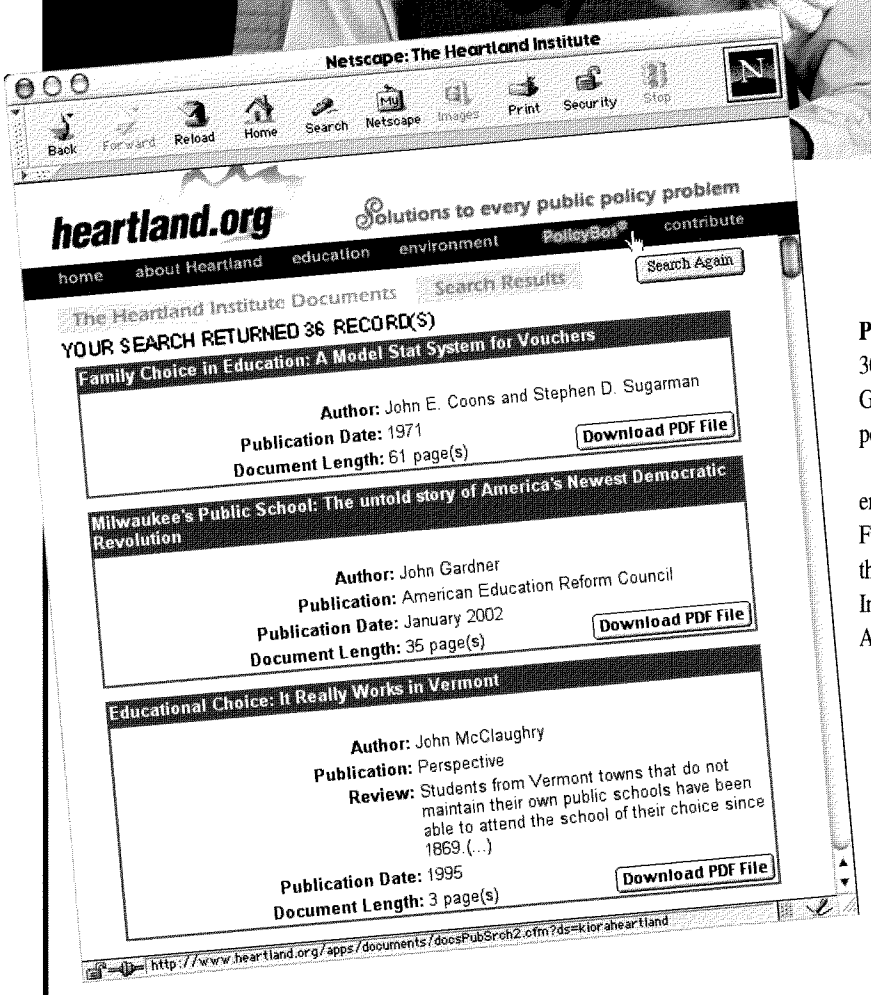

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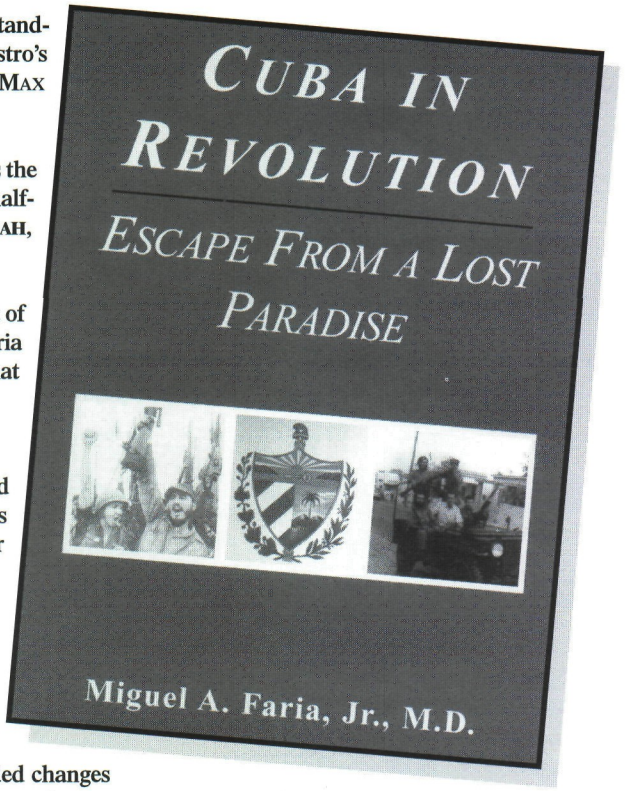

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